

Variable Annuities

If you've been offered a variable annuity, look carefully at the product to make sure it's right for you. Variable annuities sometimes are touted as "safe" investment vehicles. However, variable annuities have features that make them unsuitable for many investors.

First, find out how much commission the salesperson will earn. While salespeople should be compensated for their sales, the commissions on variable annuities can be much higher than for other retirement products, ranging from 5 to 30 percent of the investment. If the salesperson receives an up-front commission, your initial investment will be reduced by the commission rate. For example, if you have \$50,000 to invest, anywhere from \$2,500 to \$15,000 will be subtracted from your initial investment to pay the salesperson. If the salesperson will receive a trailing commission, you will be required to hold the annuity for a set period of time and may suffer significant penalties if you need to withdraw your money.

Second, variables have significant penalties if the investor needs to liquidate the investment anytime within the first three to five years of investing. For example, you may be faced with unexpected medical bills or a family emergency requiring ready cash. You may be surprised how much your initial investment has shrunk due to commission fees and surrender penalties.

Third, consumers are enticed to purchase variables because there are tax advantages. However, other investment vehicles such as IRAs and employer-sponsored 401(k) plans also provide you with tax-deferred growth and other tax advantages. For most investors it's advantageous to make the maximum allowable contributions to their IRAs and 401(k) plans before investing in a variable annuity.

And finally, if you are investing in a variable annuity through a tax-advantaged retirement plan (such as a 401(k) plan or IRA), you will get **no additional tax advantage from the variable annuity**. Under these circumstances, consider buying a variable annuity only if it makes sense because of the annuity's other features such as lifetime income payments and death benefit protection. Be especially wary if the salesperson suggests you cash out your existing IRA and invest it in a variable annuity. You may be better off keeping your investment dollars in the IRA. The tax rules that apply to variable annuities can be complicated. Before investing, you may want to consult a tax adviser about the tax consequences of investing in a variable annuity.

FACTORS TO CONSIDER WHEN PURCHASING AN ANNUITY

1. **LIQUIDITY:** Find out how long your money will be tied up. Some annuities have expensive surrender charges if you try to withdraw money before the maturity date.
2. **PRODUCT KNOWLEDGE:** Make sure you understand how the annuity works, the benefits it provides and the charges you will pay. Always demand written information about the company offering the annuity and read and understand the prospectus before investing.
3. **SUITABILITY:** Only purchase an annuity after you are satisfied it suits your investment needs and risk tolerance.
4. **RATE OF RETURN:** Watch out for introductory or teaser rates that may be significantly higher than the rate of return specified in the contract.
5. **VOLATILITY:** Some annuities involve a risk that the account value may decline if the underlying investment performs poorly.
6. **PROFESSIONAL ADVICE:** Before making a commitment to purchase an annuity, discuss the investment with your stockbroker, attorney, accountant or financial advisor.
7. **ROLLOVER:** Before cashing in one annuity to purchase another, make sure the benefits of the purchase outweigh the costs, including surrender costs, penalties and tax liabilities.
8. **OPTIONAL FEATURES:** Some annuities offer features such as long-term care insurance that will cost you extra. Consider whether you can purchase the additional benefit as a separate product at a better price.
9. **DEATH BENEFIT:** Not all annuities provide a death benefit. Understand what happens to the proceeds of your annuity upon your death.
10. **KNOW YOUR SALESPERSON:** Unscrupulous salespeople will try to scare or pressure you to buy. DO NOT DO BUSINESS WITH ANYONE WHO EMPLOYS THESE TACTICS. You should be completely comfortable with the product and the salesperson before committing any of your hard-earned money to any investment.